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## Terminal Leave Payments

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### MEMORANDUM

**TO:** Chief Financial Officers  
All Departments and Agencies

**FROM:** John J. Linderman, Director  
Office of Financial Management

**DATE:** July 22, 1997

**SUBJECT:** Terminal Leave Payments; Accounting Guidance for Expenditure and Revenue Recognition, and Policy for Allocation of Related Costs to Federal Financial Assistance Programs

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The purpose of this memorandum is to summarize the accounting guidance that should be followed in recognizing expenditures and related revenues for terminal leave payments made to former employees retiring from the State of Michigan, and to specify the State's policy for appropriate allocation of such costs to federal financial assistance programs.

### **Accounting Guidance for Recognition of Expenditures and Related Revenues for Terminal Leave Payments**

Accounting guidance for payments that are made to individuals that have terminated their employment with the State is set forth in Chapter 14-Section 2 of the Office of Financial Management (OFM) *Year-End Closing Guide*. To summarize, for those employees that were compensated through one of the governmental fund types (General and special revenue funds, mainly), agencies must record current year expenditures (and accounts payable when applicable) for the portion of the termination payments that are due and payable on or before September 30, 1997. Related revenues, if any, should also be recognized on a comparable basis. OFM will record the applicable long-term portion of the total accrued liability for termination-related payments (for all agencies) in the General Long-Term Obligations Account Group.

### **Policy for Allocation of Terminal Leave Payments to Federal Financial Assistance Programs**

*Federal Office of Management and Budget (OMB) Circular A-87* provides that terminal leave payments can be an allowable cost to federal programs. However, *Federal OMB Circular A-87* specifically states that these costs must be allocated as a "general administrative expense" to all activities of the governmental unit. *Federal OMB Circular A-87* does not permit terminal leave payments to be directly charged to federal financial assistance programs; however, the PPRISM system uses a method of direct charging programs based upon predetermined percentages of funding source and, therefore, does not meet the requirements of *Circular A-87* for purposes of allocating terminal leave payment costs.

One method for achieving an appropriate allocation is through the development of a department

level indirect cost rate negotiated with your federal cognizant agency. *However, if this approach is used, the negotiated indirect cost rate must be applied and the related federal revenues recovered from these indirect cost rates must be credited, in full, as general purpose revenue to the appropriate fund*, as required by State law. Further, recovery of such indirect federal revenues will not fully occur until after fiscal year 1996-97.

Therefore, the preferred and recommended alternative is for departments to recover the appropriate share of federal financing related to their terminal leave payments as a department level *allocated direct cost* to its various programs. If a department develops a plan to allocate its direct terminal leave costs to all of its program areas (and related financing sources), the department may credit the related federal revenue as a restricted revenue source to the appropriate fund. The allocation approach should use an appropriate basis, such as total direct salaries or FTEs, in accordance with *Federal OMB Circular A-87* and the department's specific circumstances. Each department should review the planned approach with its federal cognizant agency to obtain its approval.

Departments should not directly assign terminal leave charges to a federally cost-reimbursed program apart from a formal allocation process, without the express approval of the applicable grantor agency. This practice could lead to future audit citations and/or federal disallowances.

If you or your staff have questions regarding this memorandum, please contact Mr. Steve Stier, Director of Technical, Audit, and Business Services Division, at (517) 373-4010, or your OFM agency liaison accountant.

Approved:

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Deputy Director for Budget and  
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cc: M. Murray  
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